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No. 91-615

In the Supreme Court of the United States

OCTOBER TERM, 1991

ALLIED-SIGNAL INC.,
as successor-in-interest to
The Bendix Corporation, PETITIONER

v.

DIRECTOR, DIVISION OF TAXATION, RESPONDENT

On Writ of Certiorari to the Supreme Court of New Jersey

REPLY BRIEF OF PETITIONER ON REARGUMENT

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REPLY BRIEF OF PETITIONER ON REARGUMENT

INTRODUCTION

The position New Jersey has embraced in this case is nothing short of extraordinary. It would permit a state to tax an apportioned share of any income earned by a taxpayer even if the state has no connection with the activities that produced the income. It would define a unitary business merely by reference to ownership despite this Court's century-old admonition that a unitary business involves "something more than a mere unity of ownership." *Adams Express*, 165 U.S. at 222. At the same time, it would retain the traditional unitary business standard for combining the income of multicorporate enterprises, thereby allowing corporate form to dictate the substance of the constitutional limits on state tax power. And it would sanction multiple taxation resulting from allocation and apportionment of the same income, which this Court has explicitly condemned on the ground that "[t]axation by apportionment and taxation by allocation to a single situs are theoretically incommensurate." *Mobil*, 445 U.S. at 444.

Adoption of New Jersey's proposed regime would thus abandon the most fundamental constitutional restraints on state tax power and would foster the very evils that those restraints were designed to prevent. The Court should therefore reject New Jersey's effort to rewrite the constitutional law of state taxation and should reaffirm the sound constitutional principles underlying *ASARCO* and *Woolworth*.

I. ADOPTION OF NEW JERSEY'S EVERYTHING-IS-APPORTIONABLE REGIME WOULD JETTISON THE MOST BASIC CONSTITUTIONAL RESTRAINT ON THE EXERCISE OF STATE TAX POWER AND WOULD EFFECTIVELY OVERRULE A CENTURY OF THIS COURT'S PRECEDENTS

There is no blinking the astonishing proposition that New Jersey has advanced before this Court:

> The constitutional principle we propose is simply that when a nondomiciliary state seeks to impose its corporate net income tax on a single multistate taxpayer, . . . the . . . state has a sufficient connection with the taxpayer to include all its income in the apportionable tax base.

N.J. Rearg. Br. 27. This proposition—that "[t]he unitary business is congruent with the single corporation" (*id.*)—ignores the most fundamental limitation on state tax power and runs roughshod over scores of this Court's decisions.

First, as even New Jersey recognizes, a state's power to tax depends on the "protection, opportunities, and benefits" (*J.C. Penney*, 311 U.S. at 444) provided to the taxpayer's "*activities* in the taxing state." N.J. Rearg. Br. 9 (emphasis supplied). When a state seeks to include income from a taxpayer's out-of-state activities in its apportionable tax base, this means that "the out-of-state *activities* of the purported unitary business [must] be related in some concrete way to the in-state *activities*." *Container*, 463 U.S. at 166 (emphasis supplied). The mere fact that a corporation is subject to a state's taxing power tells us nothing about the connection of that corporation's out-of-state activities to the taxing state.[1] New Jersey's proposed test of unitariness therefore disregards the requirements of the Commerce and Due Process Clauses.[2]

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[1] The threshold nexus that subjects a taxpayer to the state's tax jurisdiction has always been viewed as discrete from the need for a connection between a taxpayer's in-state and out-of-state activities sufficient to consider the out-of-state activities in determining the taxpayer's apportionable tax base. *See, e.g., Container*, 463 U.S. at 165-66 (discussing threshold nexus question and, "[*i*]*n addition*," unitary business requirement (emphasis supplied)).

[2] Under New Jersey's approach, for example, if a single corporation owned a gambling casino in Nevada and a peanut farm in Georgia, and the operations of the two businesses had nothing to do with one another, Georgia could nevertheless include the income from the gambling casino in the taxpayer's apportionable tax base even though gambling is illegal in Georgia. Can it possibly be asserted with a straight face that Georgia has provided "opportuni-

Second, for the past 100 years the law has been clear that the mere jurisdictional presence of a taxpayer in a state does not justify the state's power to include in the taxpayer's apportionable tax base everything it owns or earns. *See, e.g., Fargo, Wallace,* and *Wells Fargo,* discussed in Allied-Signal Rearg. Br. at 11-12; *Connecticut General Life Ins. Co. v. Johnson,* 303 U.S. 77 (1938). Indeed, had the law been otherwise, the need for the unitary business principle—as a limited exception to the rule that states may not look outside their borders in exercising their tax power—would never have arisen. Once the state's jurisdiction over the taxpayer had been established, the apportionability of its tax base would have followed as a matter of course. That is not and never has been the law.

New Jersey's suggestion that its proposed rule would be consistent with the Court's prior cases (N.J. Rearg. Br. 30-33) is therefore preposterous. New Jersey's effort to distinguish the railroad property cases, which laid the constitutional foundation for the unitary business principle applied in the Court's net income tax cases (Allied-Signal Rearg. Br. 7-10), proceeds on the false premise that those cases involved "*tangible* property that can be seen and sited to a particular location." N.J. Rearg. Br. 31, n.20 (emphasis supplied); see also *id.* at 10. In fact, those cases involved taxation of *intangible* property (in *Fargo* securities, in *Wells, Fargo* bonds, in *Wallace* bonds (see Allied-Signal Br. 11-12)), and the principles adopted in those cases govern the apportionablity of income from such property, as the Court properly recognized in *ASARCO* and *Woolworth. ASARCO,* 458 U.S. at 328; *Woolworth,* 458 U.S. at 363.

New Jersey contends that, prior to the Court's decisions in *ASARCO* and *Woolworth,* "the Court applied the unitary business principle to the activities of a single corporation and invariably concluded that the single cor-

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ties, protections, and benefits" to an unrelated, out-of-state business which cannot legally be conducted in Georgia?

poration's business was indivisible." N.J. Rearg. Br. 31. This observation hardly advances New Jersey's strained attempt to square its everything-is-apportionable rule with the Court's precedents. Every one of the Court's earlier decisions involved taxpayers that were indisputably carrying on a unitary business under the familiar rule requiring an "organic connection" (*Fargo*, 193 U.S. at 499) between the taxpayer's in-state and out-of-state activities. See Allied-Signal Br. 20 n.9. Indeed, the Court's analysis in all of those cases—its search for functional ties between the corporate taxpayers' in-state and out-of-state activities—would have been wholly unnecessary had New Jersey's position been the law. Moreover, in none of those cases was any issue raised as to the apportionability of intangible income derived from activities that had no "organic connection" (*Fargo*, 193 U.S. at 499) to the taxpayer's operations in the state. New Jersey's frontal assault on the existing constitutional regime governing state taxation of multistate corporations therefore goes far beyond the overruling merely of *ASARCO* and *Woolworth*.

In fact, New Jersey's specific quarrel with the Court's opinions in those cases—that they required a unitary relationship between the payee and the payor of investment income as the exclusive test of apportionability (N.J. Rearg. Br. 7-11)—involves a point that was peripheral to their analysis of the unitary business principle and that is not even at issue here. See Allied-Signal Rearg. Br. 5 n.1. By directing its fire at the payor-payee language in *ASARCO* and *Woolworth*, New Jersey has seized on what may have been the Court's doctrinal foot fault in those cases as a pretext for dismantling the entire constitutional framework that has restrained state taxing power for over a century. The Court could easily address New Jersey's apparent concerns with *ASARCO* and *Woolworth* by explicitly recognizing the apportionability of income from intangible assets that are functionally related on a current basis to the taxpayer's trade or busi-

ness in the taxing state.[3] There is no warrant for the Court to go any further. Moreover, it is plain that Bendix's gain from the sale of its ASARCO stock would not be apportionable under such a revised interpretation of *ASARCO* and *Woolworth* because there is not—and there could not be—any claim here that Bendix employed the ASARCO stock in Bendix's day-to-day operations as working capital or used it as an asset serving an operational function under the *Corn Products* doctrine.

II. ADOPTION OF TWO DIFFERENT STANDARDS OF APPORTIONABILITY DEPENDING ON WHETHER INCOME IS EARNED BY A SINGLE CORPORATION OR BY A MULTICORPORATE ENTERPRISE WOULD ENSHRINE FORM OVER SUBSTANCE AS A PRINCIPLE OF CONSTITUTIONAL LAW

While New Jersey would ignore this Court's teaching that a unitary business involves "something more than a mere unity of ownership" (*Adams Express*, 165 U.S. at 222) for purposes of determining the apportionability of a single corporation's income, it would nonetheless retain the traditional unitary business principle for purposes of determining the apportionability of the income of a combined group of corporations. N.J. Rearg. Br. 33-34. New

[3] This would hardly be breaking new ground. See *Container*, 463 U.S. at 180 n.19. Indeed, most courts have had little problem in drawing this line. See Allied-Signal Br. 28 n.12; Allied-Signal Rearg. Br. 16 n.5. Insofar as there is any substance to New Jersey's complaint that courts have had "difficulty . . . in trying to apply the *ASARCO/Woolworth* payor-payee test in a coherent fashion" (N.J. Rearg. Br. 12-13 n.4), it is only that some courts may have taken this Court too literally in requiring a unitary relationship between the payor and the payee of intangible income as the exclusive test of the apportionability of such income. *See, e.g., Pledger v. Illinois Tool Works*, 306 Ark. 134, 812 S.W.2d 101, *cert. denied*, 112 S. Ct. 418 (1991). The Court's explicit acknowledgement of the apportionability of income from intangible assets functionally related on a current basis to the taxpayer's trade or business in the taxing state would eliminate any alleged confusion.

Jersey's approach would create the worst of both worlds: It would elevate form over substance for states like New Jersey, which strictly respect the separate corporate entity for tax purposes (N.J. Rearg. Br. 34 n.22), and it would leave intact what New Jersey labels a system based on "elusive legal concepts and lengthy factual records" (N.J. Rearg. Br. 42) for the 30 states with combined reporting provisions. 1 Multistate Corporate Income Tax Guide (CCH) ¶ 185 (1992).

The Court has made clear that the constitutionality of state taxes under the Due Process and Commerce Clauses ultimately turns on the "practical effect of a challenged tax" (*Mobil*, 445 U.S. at 443) and on "economic realities." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). Accordingly, when analyzing the apportionability of income, the Court has eschewed form as a touchstone of constitutional analysis because "the form of business organization may have nothing to do with the underlying unity or diversity of business enterprise." *Mobil*, 445 U.S. at 440. It is the "underlying economic realities of a unitary business," not the form in which it is carried on, that "affect[s] the apportionability of income." *Id.* at 441.

New Jersey's proposed taxing scheme flies in the face of these principles. To return to the example of an Illinois-domiciled corporation that operates a beauty parlor business in New Jersey and an unrelated parking lot business in California, assume that the California parking lot business is operated through a wholly-owned subsidiary. New Jersey acknowledges that it would lack the constitutional power to include the parking lot income in a combined report because there is no unitary relationship between the parking lot business and the beauty parlor business. If, however, the parking lot subsidiary were dissolved and its operations carried on by its parent, New Jersey's constitutional power would miraculously expand to include the parking lot income in the apportionable tax base because the income was all earned by a

single corporation, although the "underlying economic realities" (*id.*) remain identical.

Indeed, New Jersey's *amici* recognize the wholly formal character of the constitutional line New Jersey would draw by observing that "[a] taxpayer can control its tax exposure in New Jersey by the simple expediency of establishing wholly owned subsidiaries." Cal. Ami. Rearg. Br. 24. Thus all Bendix "had to do to avoid taxation of the disputed gain in this case was to move the ASARCO interest out into a separately organized corporation that had no nexus with New Jersey." MTC Ami. Rearg. Br. 23. While New Jersey is free as a matter of state law to adopt a scheme in which form prevails over substance, and to deny itself the right to tax constitutionally apportionable income, it cannot force feed its scheme to taxpayers by the "simple expediency" of assuming that all income earned by a single corporation is apportionable. Constitutional restraints on state tax power do not expand and contract based on economically meaningless changes in corporate organization.

This elevation of form over substance also belies New Jersey's assertion that *ASARCO* and *Woolworth* should be overruled because the definitions they draw have proven difficult to administer; under New Jersey's own approach, *ASARCO* and *Woolworth* would continue to govern in the 30 states with combined reporting provisions. 1 Multistate Corporate Income Tax Guide (CCH) ¶ 185 (1992). Those states will continue to bear "the expense and uncertainty of litigating and relitigating the unitary business issue, with each case turning on its peculiar facts." N.J. Rearg. Br. 41-42. Indeed, New Jersey might find itself pressured to adopt combined reporting if corporate taxpayers, with an expanded New Jersey tax base tied to corporate form, followed the advice of New Jersey's *amici* and altered the corporate form of their New Jersey operations to minimize their tax liability. We would then "arrive where we started and know the place for the first time." T.S. Eliot, *Little Gidding*, in *The Complete Poems and Plays* 145 (1952).

III. NEW JERSEY'S PROPOSED REGIME WOULD VIOLATE THE CONSTITUTIONAL PRINCIPLE BARRING ALLOCATION AND APPORTIONMENT OF THE SAME INCOME AND WOULD SPAWN UNACCEPTABLE LEVELS OF MULTIPLE TAXATION

New Jersey concedes that its everything-is-apportionable regime will inevitably give rise to multiple taxation if other states' laws, which generally allocate nonbusiness income to a single state (1 Multistate Corporate Income Tax Guide (CCH) ¶ 167 (1992); UDITPA §§ 5-8), are permitted to stand. N.J. Rearg. Br. 38. Faced with the Hobson's choice of impugning the constitutionality of most other states' laws, see Allied-Signal Rearg. Br. 27-29, or defending a system that will necessarily spawn widespread multiple taxation, New Jersey opted for the latter. As we demonstrate below, however, the multiple taxation resulting from New Jersey's proposed regime is constitutionally indefensible.

New Jersey fails even to mention this Court's precedents that establish the rule that precludes a domiciliary state from allocating to itself 100% of a tax base which other states have power to tax on an apportioned basis. See Allied-Signal Rearg. Br. 28. It relies instead on *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267 (1978) (N.J. Rearg. Br. 39), which held that the Commerce Clause tolerates, as the price of federalism, "some risk of duplicative taxation" occasioned by inconsistent apportionment mechanisms. 437 U.S. at 278. The risk the Court found tolerable in *Moorman*, however, was qualitatively and quantitatively different from the risk of multiple taxation created by New Jersey's proposed constitutional regime, and *Moorman* therefore provides no support for New Jersey's position.

First, all states that use apportionment formulas are attempting to determine the same thing: the share of the taxpayer's income that may be fairly attributed to the taxpayer's in-state activities. The risk of multiple taxation occasioned by the existence of varying apportionment formulas therefore is uncertain and adventitious. Incon-

sistent apportionment formulas may produce taxation of more or less than 100% of a corporation's tax base depending on the particular facts of the taxpayer's business and the particular apportionment formulas employed by the state.[4] By contrast, the risk of multiple taxation occasioned by the existence of inconsistent income attribution methods—allocation and apportionment—is absolute. With one state allocating to itself 100% of a corporation's tax base, apportionment of such income by any other state inexorably causes multiple taxation.

Second, the actuality of multiple taxation occasioned by the existence of inconsistent apportionment formulas, when it in fact occurs, is likely to be minimal, considering that no state is seeking to tax more than its fair share of the taxpayer's tax base and that most states' formulas are substantially similar. See 1 Multistate Corporate Income Tax Guide (CCH) ¶ 146 (1992). By contrast, the actuality of multiple taxation occasioned by allocation and apportionment of the same tax base will almost always be substantial, with the state to which the income is allocated taxing 100% of the taxpayer's income while other states each lay their claim to an apportioned share of the income.

New Jersey's position therefore cannot be reconciled with one of the most basic constitutional restrictions on state taxation of interstate enterprises: that two states cannot tax the same values. *Standard Oil*; *Japan Line*.

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[4] For example, the taxpayer in *Moorman*, an Illinois-based manufacturer selling into Iowa, complained that the application of Iowa's single-factor sales formula, in conjunction with Illinois' standard three-factor formula of property, payroll, and sales, subjected it to taxation on more than 100% of its income from Iowa sales. Iowa would tax all of such income based on sales into Iowa while Illinois would tax a portion of it based on the taxpayer's property, payroll, and sales in Illinois. By the same token, however, an Iowa-based manufacturer selling into Illinois would be subjected to taxation on less than 100% of its income from Illinois sales. Iowa would tax none of such income because there are no Iowa sales while Illinois would tax only a portion of it based on the taxpayer's property, payroll, and sales in Illinois.

It therefore is not surprising that the Court already has flatly rejected New Jersey's position here, declaring that "[t]axation by apportionment and taxation by allocation to a single situs are theoretically incommensurate." *Mobil*, 445 U.S. at 444. While acknowledging the power of a domiciliary state to lay "some" tax upon the income of a unitary business conducted in the state, the Court declared that "there is no reason in theory why that power should be exclusive" when the income derives "from a unitary business, part of which is conducted in other States." *Id.* at 445-46. In short, the Court has made clear that it will not tolerate the multiple taxation that could result from "theoretically incommensurate" claims to allocation and apportionment of the same income. *Id.* at 447; Allied-Signal Rearg. Br. 27-29.

Beyond the analytical flaws in New Jersey's defense of multiple taxation, its attempt to downplay the magnitude of the problem on the ground that "allegations of double taxation of intangible income are relatively infrequent" (N.J. Rearg. Br. 38 n.27 (citing Appendix)) is misleading and disingenuous. First, in a number of cases cited by New Jersey, taxpayers in fact did raise issues of multiple taxation.[5] Second, and more significantly, since New Jersey's scheme envisions the apportionment of all income —whether derived from tangible or intangible assets— the citation of cases involving only intangible income does not begin to portray the extent of multiple taxation that would result from New Jersey's approach. For example, if a taxpayer owns real property unrelated to its business

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[5] *See W.R. Grace & Co. v. Commissioner of Revenue*, 393 N.E.2d 330, 337 (Mass. 1979); *Great Lakes Pipe Line Co. v. Commissioner of Taxation*, 138 N.W.2d 612, 619 (Minn. 1965), *appeal dismissed*, 384 U.S. 718 (1966); *Qualls v. Montgomery Ward & Co.*, 585 S.W.2d 18, 31 (Ark. 1979) (overruled by *Pledger v. Illinois Tool Works, Inc.*, 812 S.W.2d 101 (Ark.), *cert. denied*, 112 S. Ct. 418 (1991)); *Lone Star Steel Co. v. Dolan*, 668 P.2d 916, 927 (Colo. 1983) (*en banc*); *NCR Corp. v. Commissioner of Revenue*, 438 N.W.2d 86, 94 (Minn. 1989), *cert. denied*, 493 U.S. 845 (1990).

operations, most states will allocate the capital gain from the sale of such property to the state where the property is located. *See, e.g.*, UDITPA § 6(a). If, as New Jersey urges, it were constitutionally permissible for states to apportion nonbusiness income from sales of real property located in other states, multiple taxation would inevitably result.[6]

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[6] Even if the Court believed it was relevant to inquire why the issue of double taxation may not have arisen in some of the cases cited by New Jersey in its Appendix, there are good explanations, none of which even remotely justifies the regime of extensive multiple taxation that New Jersey would have this Court endorse. Almost all of the non-New Jersey cases fall into one or both of the following two categories: (a) the laws of the state of commercial domicile did not provide for allocation of the class of income that was at issue, so there was no risk of double taxation, *see James v. International Tel. & Tel. Corp.*, 654 S.W.2d 865 (Mo. 1983) (*en banc*) (New York); *M. Lowenstein Corp. v. South Carolina Tax Comm'n*, 378 S.E.2d 272 (S.C. Ct. App. 1989) (New York); *Corning Glass Works, Inc. v. Virginia Dep't of Taxation*, 402 S.E.2d 35 (Va.), *cert. denied*, 112 S. Ct. 277 (1991) (New York); *Philip Morris, Inc. v. Director of Revenue*, 760 S.W.2d 888 (Mo. 1988) (*en banc*) (New York); *American Home Prods. Corp. v. Limbach*, 551 N.E.2d 201 (Ohio), *cert. denied*, 111 S. Ct. 63 (1990) (New York); *Champion Int'l Corp. v. Bureau of Revenue*, 540 P.2d 1300 (N.M. 1975) (Connecticut); *Comptroller v. Armco, Inc.*, 521 A.2d 785 (Md. Ct. Spec. App. 1987) (Ohio); *NCR Corp. v. Comptroller of the Treasury*, 544 A.2d 764 (Md. 1988) (Ohio); *NCR Corp. v. South Carolina Tax Comm'n*, 402 S.E.2d 666 (S.C. 1991) (Ohio); and/or (b) the taxpayer won on other grounds, so so that the court never had to reach the issue of double taxation. *See James v. International Tel & Tel. Corp.*, 654 S.W.2d 865 (Mo. 1983) (*en banc*); *Corning Glass Works, v. Virginia Dep't of Taxation*, 402 S.E.2d 35 (Va.), *cert. denied*, 112 S. Ct. 277 (1991); *Philip Morris Inc. v. Director of Revenue*, 760 S.W.2d 888 (Mo. 1988) (*en banc*); *Brunner Enters. v. Department of Revenue*, 452 So. 2d 550 (Fla. 1984); *Pledger v. Illinois Tool Works, Inc.*, 812 S.W.2d 101 (Ark.), *cert. denied*, 112 S. Ct. 418 (1991); *Jewel Companies, Inc. v. Department of Revenue*, No. CT-1985-4 (1990 Mont. Tax LEXIS 81), remanded Montana First Judicial District Court No. BDV-89-294 (Oct. 31, 1991); *American Home Prods. Corp. v. Limbach*, 551 N.E.2d 201 (Ohio), *cert. denied*, 111 S. Ct. 63 (1990).

IV. THE CONSTITUTIONAL REGIME ESPOUSED BY NEW JERSEY AND ITS *AMICI* IS ESSENTIALLY A REGIME WITH NO MEANINGFUL RESTRAINTS ON STATE TAX POWER

What New Jersey wants, in the end, is a regime in which states are free to tax income in any way they please subject only to nominal constitutional restraints. It wants a world in which a state may include all of a nondomiciliary's income in its apportionable tax base without any inquiry into the link between the activities that produced the income and the taxing state. N.J. Rearg. Br. 27. It wants a world in which other states have similar latitude in choosing apportionment methods, including methods that will inevitably result in multiple taxation when employed alongside its own. *Id.* at 40-41. And it wants a world in which such multiple taxation may be imposed with constitutional impunity. *Id.* at 38-40.

New Jersey's *amici* are of the same mind. See Cal. Ami. Rearg. Br.; Conn. Ami. Rearg. Br.; MTC Ami. Rearg. Br. Indeed, in this respect the audacity of the Multistate Tax Commission's (MTC's) brief is remarkable. The MTC is the "administrative arm" of the Multistate Tax Compact, which seeks to "promote uniformity or compatibility of state tax systems . . . and avoid duplicative taxation" (MTC Opening Br. 1-2); the MTC describes as its "central" goal "[f]ostering state tax uniformity." *Id.* at 2-3. Yet the MTC wholeheartedly endorses New Jersey's effort to tax all intangible income on an apportioned basis, despite the inconsistency of New Jersey's position with UDITPA, which the MTC administers, and the duplicative taxation it will inevitably cause.[7]

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[7] While the MTC calls for a "practical, even-handed statement of the unitary business principle," MTC Ami. Rearg. Br. 2, it is later apparent that the "new" unitary business principle permits full apportionment of income from intangibles. *Id.* at 18-23. Although described at one point as a "statutory presumption," it is clear that it is not rebuttable. *Id.* at 21.

The MTC also seeks to justify New Jersey's everything-is-apportionable regime on the ground that New Jersey accepts "the good and the bad of its choice." MTC Ami. Rearg. Br. 22. By "bad" the MTC means that New Jersey has "forego[ne] complaint," permitting non-New Jersey losses to reduce New Jersey income, where a taxpayer incurs such losses from a business segment that "operate[s] distinctly" from the business operating in New Jersey. *Id.*[8] However, our constitutional system is not one in which the unconstitutional extraterritorial taxation of Taxpayer A becomes justifiable because the tax collector undercollects from Taxpayer B.

Finally, the MTC fails in its attempt to define a workable unitary business principle by reference to an amorphous standard of business purpose linking operationally unrelated business activities on the basis of "the existence of management that is organized or poised to ensure that individual business segments operate for the benefit of the integrated whole." *Id.* at 9. This is simply a recycled version of the contentless unitary business standard adopted by the court below and the meaningless "corporate purpose" standard of a unitary business rejected by the Court in *ASARCO* and *Woolworth.* Indeed, it was New Jersey's very inability to articulate a meaningful line based on such unintelligible criteria that induced it to invite the Court to discard the unitary business principle altogether.

It is also worth noting that New Jersey, while acknowledging the "theoretical uncertainty" and "practical problems" that its taxing regime would create with respect to

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[8] The MTC does acknowledge that "in a rare circumstance" there may be different segments in a business that operate distinctly, but this does not change its support of New Jersey even in those circumstances. *Id.* Indeed, in responding to our beauty shop/parking lot hypothetical, which involved two businesses that were as unrelated as we could make them, the MTC could not resist "fighting the hypothetical" by fabricating various "transfer[s] of value" (*id.* at 9) between the businesses that did not in fact exist. *Id.* at 8-9.

fair apportionment, offers the Court no solution to these problems. N.J. Rearg. Br. 37; see Allied-Signal Rearg. Br. 25-27, 31-33. Allied Signal and its *amici* have addressed these problems in detail and have argued that the difficulty in solving them is just one more reason for the Court to maintain the existing constitutional regime for apportioning and allocating corporate income. New Jersey's leave-it-to-another day attitude (N.J. Rearg. Br. 37) reflects its own inability to provide satisfactory answers and reinforces Allied-Signal's position here.

Even if the Court were not otherwise persuaded of the wrongheadedness of New Jersey's proposed "solution" to the problems of dividing the income of multistate businesses,[9] the mischievous practical consequences flowing from New Jersey's proposed regime militate against the abandonment of the existing constitutional structure. Two-thirds of the states' laws would be put in immediate constitutional jeopardy or, alternatively, there would be dramatic increases in multiple taxation. Allied-Signal Rearg. Br. 27-30. The problem of fair apportionment would be greatly exacerbated, as taxpayers and tax administrators struggled with the question of how to conform apportionment formulas to a radically expanded tax base. *Id.* at 25-27. And the potential for gross misattribution of income would increase dramatically, as would the lower courts' (and this Court's) entanglement with state tax apportionment. *Id.* at 31-33.

Against this background, it is all the more remarkable that New Jersey asks the Court to overrule *ASARCO* and

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[9] There is one additional error in New Jersey's brief that requires correction. New Jersey declares that "Bendix reported the ASARCO investment on the equity method . . . thereby indicating to the public that it had the ability to exercise significant influence over ASARCO." N. J. Rearg. Br. 45 n.32. This statement is simply wrong. Reporting on the equity method requires only that the shareholder own more than 20% of the corporation's stock; it is a purely mechanical test. Stip. ¶ 55 (J.A. 168). Moreover, the stipulated facts are that "Bendix did not exert any control over ASARCO." Stip. ¶ 54 (J.A. 168).

Woolworth without advancing any of the factors that traditionally have been understood to justify a departure from the principles of *stare decisis*. New Jersey fails even to suggest that *ASARCO* and *Woolworth* are inconsistent with other decisions of this Court. The State does not attempt to demonstrate that action by the Court is necessary " 'to bring its opinions into agreement with experience and with facts newly ascertained.' " *Vasquez*, 474 U.S. at 266 (citation omitted). And the disharmony in the lower courts asserted by New Jersey (a disharmony that, we show above, is in any event illusory (see p. 5 n.3)) would not be cured by New Jersey's proposed scheme; to the contrary, the State's approach would introduce an entirely new set of concededly intractable problems that would engender widespread confusion and extensive litigation. In these circumstances, New Jersey has not carried the "severe burden" imposed by the doctrine of *stare decisis* "on the litigant who asks [the Court] to disavow one of [its] precedents." *Thomas*, 448 U.S. at 272 (plurality opinion).[10]

V. IF *ASARCO* AND *WOOLWORTH* ARE OVERRULED, THE DECISION SHOULD NOT BE RETROACTIVE

There is one proposition that both parties and all of the *amici* that address the question accept: that the test of *Chevron Oil Co. v. Huson*, 404 U.S. 97 (1971), should determine whether a decision overruling *ASARCO* and *Woolworth* is retroactive. This unanimity on the part of taxpayers and taxing officials—even those whose short-term interests in this case might be furthered by a rule of absolute retroactivity—is a powerful reminder that

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[10] The list of Commerce Clause decisions that the Court has discarded in recent years, which are cited by New Jersey at Rearg. Br. 7 n.1, simply adds emphasis to the weakness of its argument in this case; all of those decisions were overruled in the wake of the Court's landmark holding in *Complete Auto*, which worked a dramatic change in the Court's analytical framework. There has, of course, been no such change in the unitary business principle since the decisions in *ASARCO* and *Woolworth*.

stability in the law is highly valued by all segments of society. While we agree with New Jersey on that point, however, the State unfortunately does not demonstrate the same good sense in its *application* of the three-part *Chevron Oil* test.

1. New Jersey (see N.J. Rearg. Br. 17-18) and several of its *amici* suggest that a decision overruling *ASARCO* and *Woolworth* would not "establish[] a new principle of law . . . by overruling clear past precedent" within the meaning of *Chevron Oil*'s first prong because the holdings in those decisions were undercut by the Court's subsequent ruling in *Container Corp.* v. *Franchise Tax Board*, 463 U.S. 159 (1983). That contention is wholly without substance. Citing *ASARCO* (among many other cases), the *Container* Court expressly *affirmed* the proposition that is dispositive here: "that the out-of-state activities of the purported 'unitary business' [must] be related in some concrete way to the in-state activities"—a connection that requires something beyond "the mere flow of funds arising out of a passive investment or a distinct business operation." *Id.* at 166.

At the same time, the *Container* Court's lengthy discussion of *ASARCO* and *Woolworth* did not retreat from the holdings of those decisions in any manner that is relevant here. To the contrary, the Court quoted extensively from *Woolworth* in observing that " '[s]ubstantial mutual interdependence' " between components of a business is necessary to support a finding of unitariness (463 U.S. at 179, quoting 458 U.S. at 371); "that a unitary business finding could not be based merely on 'the type of occasional oversight—with respect to capital structure, major debt, and dividends—that any parent gives to an investment in a subsidiary' " (463 U.S. at 180 n.19, quoting 458 U.S. at 369); and that the parent in *Container* provided assistance and supervision to its subsidiaries that far exceeded any such connection in *ASARCO* and *Woolworth*. 463 U.S. at 179. Indeed, the

Court's opinion in *Container*, issued just a year after *ASARCO* and *Woolworth* were decided, was written by Justice Brennan and joined by Justices White and Marshall, all of whom also were in the majority in *ASARCO* and *Woolworth*. It is hardly likely that they intended *Container* to work a major departure from those holdings—or that taxpayers would have understood it to do so.[11]

2. New Jersey also asserts (N.J. Rearg. Br. 20) that retroactivity is mandated by the second prong of the *Chevron Oil* test because "[i]t would not further the new rule of law if New Jersey were to prevail but at the same time forfeit the revenue riding on the pending cases." But if that were a proper understanding of *Chevron Oil*, the second prong *always* would dictate retroactivity; under the State's approach, the purpose of the rule at issue necessarily is advanced by giving it effect into the past. In fact, the Court never has applied its test in such a circular fashion. Instead, as we explained in our opening brief on reargument (at 46), the Court has looked to whether retroactivity will help ensure compliance with its decisions and otherwise will advance particular federal policies. New Jersey has offered no reason to believe that to be the case here.

3. Finally, New Jersey contends (at N.J. Rearg. Br. 18-20) that the equities cut against retroactivity (and that there could not have been the reliance on past law that is an element of the first prong of the *Chevron Oil* test) because Bendix's acquisition and sale of ASARCO stock predated the decisions in *ASARCO* and *Woolworth*. This argument, of course, is premised on the assumption that *ASARCO* and *Woolworth* stated novel principles of law. But that is not so; we demonstrate above both that the

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[11] As we explain above (at p. 5 n.3), the state cases cited by New Jersey (at N.J. Rearg. Br. 17) as demonstrating confusion about the meaning of *ASARCO* and *Woolworth* did not, in fact, exhibit uncertainty on any point relevant here.

specific holdings of those cases had long before been anticipated in decisions like *Fargo* and *Wallace*, and that the Court *never* has embraced the "unity of ownership" theory that New Jersey advances here. Accordingly, the overruling of *ASARCO* and *Woolworth* on the grounds urged by New Jersey would involve a rejection of principles upon which taxpayers have relied for a century.

More generally, New Jersey simply urges the wrong inquiry when it looks to the circumstances of the particular litigants before the Court rather than the equities as they apply to *all* taxpayers and taxing authorities who would be affected by retroactivity. The State's narrower focus would have one of two consequences: either it would require that the retroactivity of a decision be settled as to everyone by the fortuitous balancing of the equities in the first case to reach the Court, or it would require the Court to apply different rules of law to different parties depending upon their particular circumstances. Neither of these approaches is palatable. The first is simply irrational. And the second, as Justice Souter recently explained, is inconsistent with basic notions regarding consistency in the rule of law:

> Nor . . . are litigants to be distinguished for choice-of-law purposes on the particular equities of their claims to prospectivity: whether they actually relied on the old rule and how they would suffer from retroactive application of the new. It is simply in the nature of precedent, as a necessary component of any system that aspires to fairness and equality, that the substantive law will not shift and spring on such a basis. . . . The applicability of rules of law are not to be switched on and off according to individual hardship; allowing relitigation of choice-of-law issues would only compound the challenge to the stabilizing purpose of precedent posed in the first instance by the very development of 'new' rules. Of course, the generalized enquiry permits litigants to assert, and the courts to consider, the equitable and

reliance interests of parties absent but similarly situated.

James B. Beam Distilling Co. v. Georgia, 111 S. Ct. 2439, 2447-2448 (1991) (opinion of Souter, J.).[12]

New Jersey makes no attempt to conduct such a generalized inquiry here. While it suggests (at N.J. Rearg. Br. 20 n.13) that taxpayers in UDITPA states might find some protection in existing state law limits on apportionment, the State simply disregards the effects of retroactivity on the many taxpayers in states like New Jersey, which have had statutes purporting to permit the taxation of intangible non-operational income; New Jersey would disrupt the expectations of such taxpayers so that the states could receive payments that "they had no reason to anticipate." *James Beam*, 111 S. Ct. at 2455 (O'Connor, J., dissenting). And New Jersey wholly ignores the impact of its approach on the UDITPA states themselves, which would be opened to potentially devastating refund lia-

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[12] This appears to be the view of a majority of the Court. A plurality of the Court in *James Beam* was of the view that, "[o]nce retroactive application is chosen for any asssertedly new rule, it is chosen for all others who might seek its prospective application." 111 S. Ct. at 2447-2448 (opinion of Souter, J.). See *id.* at 2448-2449 (White, J., concurring in the judgment). As a consequence, Justice Souter proposed use of a generalized inquiry to avoid having retroactivity as to all determined by the peculiar circumstances of the first litigant. See *id.* at 2447 (opinion of Souter, J.) ("Because the rejection of modified prospectivity precludes retroactive application of a new rule to some litigants when it is not applied to others, the *Chevron Oil* test cannot determine the choice of law by relying on the equities of the particular case"). The *James Beam* dissenters, while reasoning that the retroactivity question should not be regarded as settled when the first case to apply the new rule did not use the *Chevron Oil* test (see *id.* at 2451-2452 (O'Connor, J., dissenting)), appeared to accept the proposition that *Chevron Oil's* balancing of the equities requires a generalized inquiry. See *id.* at 2455 (O'Connor, J., disssenting) (emphasis added) (noting effect of retroactivity on "James Beam and *other liquor manufacturers*," and "on Georgia *and the other States* that reasonably relied on this Court's established precedent").

bility by a retroactive overruling of *ASARCO* and *Woolworth*. See Allied-Signal Rearg. Br. 29 n.13. In these circumstances, the equities—as well as the other elements of the *Chevron Oil* test—would mandate a holding of non-retroactivity.

CONCLUSION

For the foregoing reasons and the reasons expressed in our earlier briefs in this case, the judgment of the New Jersey Supreme Court should be reversed.

Respectfully submitted,

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